

Weekly Review<?xml:namespace prefix = o ns =
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While it felt like silver prices were under pressure most of the week, we actually closed up about 50 cents, while gold declined about \$12. Thus, silver recorded its second highest weekly close in 30 years. Importantly, the gold/silver ratio tightened in to close at another multi-year milestone of just over 47. As you know, I have been beating the drum to switch from gold into silver for quite some time and I would like to pass along an observation that may set you back a bit. It certainly set me back when my friend and mentor Izzy Friedman pointed it out to me.

As I have written previously, most people have trouble relating to changes in the gold/silver ratio because the numbers don't mean a great deal to them. After all, what does it mean to the average person that the gold/silver ratio tightened in from 66 in August to 47 today? Not much, and that's why I suggest not looking at the ratio change exclusively. Here is what Izzy pointed out to me. If gold had kept pace with the price move we have witnessed in silver since August, meaning the ratio remained at 66, the price of gold today would be \$1927 ($66 \times \29.20), or \$550 higher than the current gold price of \$1376.

I don't know about you, but that calculation shocked me. I mean, I knew silver

had done much better than gold over the past 4 months, but not to that extent. Or let me put it differently. If someone had not switched from gold into silver back in August, he would have only had the same investment return by not switching into silver had gold rallied \$550 to \$1927. Obviously, we can't turn the clock back to August and get a second chance to do the switch at a 66 ratio today, but the circumstances still strongly suggest to me that silver will continue to outperform gold. Remember, I'm talking about a non-margined switch from gold to silver, not a leveraged gold/silver spread. (Although such a trade would have been spectacular to date, there is too much risk when you employ too much leverage).

Another drumbeat has been developments in the silver wholesale physical market, where turnover and movement have been frantic. We have been seeing almost daily movements in and out of the COMEX silver inventories and the big silver ETF, SLV, of 1.5 to 2 million ounces. These are extraordinary quantities of silver being moved around and are strongly suggestive of extreme tightness. It still feels to me that this tightness is pointing to a growing silver shortage due to higher than usual demand.

The latest Commitment of Traders Report (COT) indicated a reduction in the total commercial net short position in both silver and gold. Gold saw a bigger total improvement than silver, but what stood out in silver was a notable reduction of 1900 contracts in the big 4 category. Simply put, JPMorgan appears

to have been the buyer. The big 4 COMEX silver shorts now hold their smallest net short position since May 2009. At 42,167 contracts (a bit over 210 million ounces) the position is still manipulatively large with much room for more buying back. But the trend is clear □ JPMorgan wants out of its silver short position.

My guess is that JPMorgan is down to a net COMEX short position of 24,000 contracts (120 million ounces), their lowest short position in more than a year and a half, and close to the lowest levels since they acquired the Bear Stearns concentrated short position in March 2008. The only difference is that when JPM held its lowest short positions previously (22, 000 to 23,000 contracts), that was when silver was \$9 to \$12, after they had succeeded in manipulating prices sharply lower. This time, the price of silver is at \$29, meaning that JPM has been buying back at much higher prices than ever before. I believe this is not an accident and implies that JPMorgan wants out of its silver short position at almost any cost. This seems reasonable considering the incredible negative publicity that their involvement in silver has generated. It goes without saying that I don't think JPMorgan will meaningfully increase their silver short position ever again. That has been and will be super-bullish for the price.

Tallying up all the normal factors normally reviewed in silver, such as physical and market structure considerations, the price could really rock and roll to the upside. Throw in regulatory developments and it seems even more so. As

always, we must strive to keep things in perspective. While the silver manipulation has yet to have the wooden stake driven through its heart, we're much closer to that eventuality. Besides, it's easier to demonstrate some more patience on the matter, as waiting with silver at 30 year highs and up six fold from the lows is not a painful experience.

A few words on my article yesterday reviewing the Dec 16 CFTC open hearing. I hope I was clear that I viewed what occurred in a very positive light. I believe that the Commission, and especially the surveillance and oversight staff, has a new understanding of what has been transpiring in the silver market in regards to the concentrated short position. I believe they should know what to do next and dig into the details of the counterparties of JPMorgan's OTC swap positions, something the CME has been negligent in doing. Perhaps my optimism is misplaced, but it should become obvious fairly soon what the agency intends to do. I am still struck by how resistant the CME has been to any meaningful regulatory reform, considering their self-regulatory organization responsibilities. As I was viewing Thursday's hearings on the web, the chairman of the CME was on CNBC arguing against any change at all in position limit regulation. It just seemed disrespectful to me.

A number of you have inquired about my speculation that it may be Chinese counterparties on the short side of the OTC silver swaps assumed by me to be held long by JPMorgan. The gist of the queries center on what possible

motivation would Chinese interests have in being short silver, especially since there have been many reports of China's government encouraging its citizens to buy silver and gold. Please remember it is not so important who the counterparties are, but what is the legitimacy of their holding a concentrated OTC silver short position that is being transferred to the COMEX.

I did not pick interests in China out of the thin air. As the largest producer of silver in the world (mine plus refining), it would sound plausible for them to be short (but never to the extent it has reached on their surrogate COMEX position held by JPM). More importantly, rogue traders from China have had a regular habit of betting on the short side of world commodities that their country consumes with a ravenous appetite, although that would not appear to make sense. Two examples that come to mind are disastrous bets on the short side of oil and copper 5 or six years ago.

http://www.investmentrarities.com/ted_butler_comentary/12-07-04.html

<http://www.economist.com/node/5164898>

I agree that it made no sense for Chinese traders to have bet the short side big in oil or copper. Yet it happened. Just because it makes no sense for someone from China to have bet big on the short side of silver doesn't mean it couldn't also happen. Let's face it □ someone is and has been short on silver, all the way up from the single digits. It will go down as the single dumbest trade in history

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when all is said and done, taking the title away from Barrick Gold and Anglo Ashanti for their dumb short gold trades. Sooner or later, all the details of the silver short will come out and we won't have to speculate. Until that time, I'll stick with my speculation.

Ted Butler

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Silver - \$29.20

Gold - \$1376